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S E C R E T VALLETTA 000517

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SUBJECT: MALTA AGREES TO DENY REQUESTS BY IRANIAN BANKS TO ESTABLISH SUBSIDIARIES IN MALTA

REF: A. SECSTATE 115523
1B. VALLETTA 485

Classified By: DCM Jason L. Davis for reasons 1.4 (b) and (d)

¶1. (U) On December 11, DCM called on MinFin Head of Secretariat Alan Caruana to get the GoM's formal response to Ref A demarche, which asked that Malta agree to adopt "at least one" of several proposed "preventative measures to address the specific risks posed by Iran."

¶2. (C) The text of the GoM's response, drafted by Malta's Financial Intelligence Analysis Unit (FIAU), appears at paragraph 5, below. One highlight is a firm commitment by Malta to deny requests by Iranian banks to establish a subsidiary, branch, or representative office in Malta. The mechanism for denial is based on a determination by the Malta Financial Services Authority (MFSA) that "nationals or institutions from Iran would not be considered by the MFSA as being fit and proper persons for the purposes of MFSA's licensing criteria." In fact, the FIAU report noted, MFSA had recently discouraged a potential request for the establishment in Malta of a representative office of an Iranian credit institution.

¶3. (C) The FIAU report also noted that Malta was already implementing several of the other measures proposed in the demarche, including requiring Maltese financial institutions to identify clients and beneficial owners before establishing business relationships with individual companies from Iran, reviewing existing account relationships based on risk assessment, and imposing enhanced reporting requirements for financial transactions involving Iran.

¶4. (S) One disappointing element to the report was the response to our proposal that Malta deny requests by Iranian institutions to enter into joint ventures with or purchase a controlling stake in any local financial institution. On this point there was no firm commitment to prevent it, only an assertion that the MFSA did have the authority to deny such requests, and that existing statutory criteria were robust enough to enable the MFSA to adequately verify the risks to the local financial system posed by such requests. DCM asked Caruana whether he thought the FIAU had deliberately left the door open to such acquisitions, and if so why. Caruana recommended that he, Ambassador Bordonaro, and DCM meet with the FIAU leadership to ask this question and to push for improved language. A meeting is being scheduled for early January, in order to accommodate the travel schedules of the relevant officials.

¶5. (SBU) Following is the text of the GoM's response to Ref A demarche:

Begin Text

JOINT NOTE PREPARED BY THE FINANCIAL INTELLIGENCE ANALYSIS UNIT AND THE MALTA FINANCIAL SERVICES AUTHORITY

Preventive measures adopted by the Financial Intelligence Analysis Unit (&FIAU8) and the Malta Financial Services Authority (&MFSA8) pursuant to the FATF Statement issued on

the 16th October 2008 (&the October Statement8) and the FATF Guidance on the implementation of financial provisions of UN Security Council Resolution 1803 issued on the 17th October 2008 (&the Guidance8).

FATF October Statement

The FIAU, as the entity responsible in Malta inter alia for the dissemination of information with a view to combating money laundering and the financing of terrorism, took immediate steps to ensure that the October Statement be brought to the attention of all subject persons in terms of the Prevention of Money Laundering and Funding of Terrorism Regulations, 2008 ("the 2008 Regulations").

Indeed, the approach adopted by the FIAU was similar to that taken with regard to the previous Statement issued by the FATF on 28th February 2008. The October Statement was in fact prominently placed on the FIAU's website and circulated to all credit and other financial institutions individually with a note to take measures to ensure compliance thereto.

As to the other persons falling within the scope of the Maltese AML/CFT laws, the FIAU forwarded the October Statement to all the representatives of subject persons sitting on the Joint Committee for the Prevention of Money Laundering and Funding of Terrorism. This Committee is composed of associations and bodies representing subject persons, together with the Police, the Attorney General's Office, the MFSA and the Central Bank of Malta. The members of the Committee were asked to circulate the October Statement and to bring its contents to the notice of all their members.

FATF Guidance re UNSCR 1803

In the case of the Guidance, the FIAU took similar measures to bring this document to the attention of the industry whilst making sure that it itself applies that guidance related to the authorities. Thus the FIAU has notified all credit institutions individually with respect to the Guidance and encouraged them to examine and apply all the measures laid out therein. The Guidance has also been prominently placed on the FIAU's website.

Other Measures

Other measures adopted in relation to the October Statement and the Guidance by the FIAU as the regulatory authority on money laundering and financing of terrorism issues, and by the MFSA, as the regulatory authority responsible for the supervision of credit and financial institutions in Malta, are highlighted in the paragraphs below in sequence to the request.

(A) Client and beneficial owner identification before the establishment of business relationships with individuals or companies from Iran

In line with the FATF 40 Recommendations and the relevant EU Directives, Maltese financial institutions are prohibited by the 2008 Regulations from forming a business relationship with a person unless the financial institution adopts adequate customer due diligence measures and maintains adequate records. Such measures include among other things the identification and verification of the identity of the individual seeking to establish a business relationship and, where relevant, that of the beneficial owners. Additionally, as part of its ongoing monitoring obligations, the financial institution must keep its information up to date. These obligations exist irrespective of the nationality of the client.

Moreover, subject persons are required to apply, on a risk-sensitive basis, enhanced customer due diligence measures in situations which, by their nature, can present a higher risk of money laundering or the funding of terrorism. Consequently, in view of the issuance of the above-mentioned

Statement and previous similar statements, subject persons are expected to apply enhanced due diligence measures where applicants for business are Iranian nationals, Iranian companies or have close connections with Iran.

Subject persons who breach the obligations of identification and verification of the person seeking to establish a business relationship or who do not apply the customer due diligence requirements established by the 2008 Regulations may be subjected to the imposition of administrative penalties by the FIAU.

(B) Review of existing correspondent account relationships based upon a risk assessment in order to determine whether the respondent Iranian financial institutions are complying with relevant requirements.

Notwithstanding that EU Regulations are binding on member states without the need for transposition into national legislation, the Malta Financial Services Authority (&MFSA8) in June 2008 issued a circular to licensed credit institutions drawing attention to the EU Commission Regulation (EC) No 219/2008 of 11 March 2008 amending Council Regulation (EC) No 423/2007 concerning restrictive measures against Iran and on Council Decision (2008/475/EC) implementing Article 7(2) of Regulation (EC) No 423/2007. Credit institutions are therefore required to undertake correspondent banking relationships in line with the requirements of the afore-stated EU Regulations. Additionally, during on-site reviews conducted at local banks, supervisory inspectors acting also as agents of the FIAU, undertake the necessary analyses to verify that the institutions are abiding with these (and other) statutory requirements and check as part of their oversight that no relationship would have been entered into with the individuals/persons mentioned in the Regulations.

Moreover, Regulation 11(3) of the 2008 Regulations provides that credit institutions and electronic money institutions establishing cross-border correspondent banking and other similar relationships with respondent institutions from a country other than a Member State of the European Community are required to ensure that they fully understand and document the nature of the business activities of their respondent institution, including, from publicly available information, the reputation of and the quality of supervision on that institution and whether that institution has been subject to a money laundering or funding of terrorism investigation or regulatory measures. In such circumstances, the credit institutions and electronic money institutions would also be required to assess the adequacy and effectiveness of their internal controls for the prevention of money laundering and the funding of terrorism, to obtain the prior approval of senior management for the establishment of new correspondent banking relationships, to document their respective responsibilities for the prevention of money laundering and the funding of terrorism and, in the case of payable-through accounts, they are expected to be satisfied that the respondent credit institution has verified the identity of and performed on-going due diligence on the customers having direct access to the accounts of the respondent institution and that it is able to provide relevant customer due diligence data to that subject person upon request.

(C) Enhanced reporting requirements for financial transactions involving Iran

Subject persons are required by Regulation 15(1) of the 2008 Regulations to examine with special attention, and to the extent possible, the background and purpose of any complex or large transactions, including unusual patterns of transactions, which have no apparent economic or visible lawful purpose and any other transactions which are particularly likely, by their nature, to be related to money laundering or the funding of terrorism, to establish their findings in writing and to make such findings available to the FIAU and to the relevant supervisory authorities in

accordance with applicable law.

In addition, subject persons are required, pursuant to Regulation 15(2) of the 2008 Regulations, to pay special attention to business relationships and transactions with persons, companies and undertakings carrying out their activity from a jurisdiction that does not meet the criteria of a & reputable jurisdiction⁸ i.e. a country having appropriate legislative measures for the prevention of money laundering and funding of terrorism and that complies with internationally accepted standards for the prevention of money laundering and for combating the funding of terrorism. In this regard, the October 2008 Statement and other similar FATF statements are seen to constitute valid tools in determining whether a jurisdiction is to be considered reputable or otherwise.

It is important to point out that, as the US Authorities had already been informed in April 2008 in a meeting with Mr Stuart Levey, US Under Secretary of the Treasury for Terrorism and Financial Intelligence, a credit institution which had in the past carried out transactions with Iranian entities and individuals was asked by the MFSA to submit detailed information relating to its exposures to these entities. The information is being actively monitored and this credit institution is in regular contact and updating the authorities with developments in this area.

(D) Restrict financial transactions with Iran or persons in Iran;

In accordance with Regulation 15(3) of the 2008 Regulations, where a jurisdiction which is deemed non-reputable continues not to apply measures equivalent to those laid down by the 2008 Regulations, subject persons are required to inform the FIAU. In such cases the FIAU, in collaboration with the relevant supervisory authority, may require such business relationship not to continue or a transaction not to be undertaken or apply any other counter-measures as may be adequate under the respective circumstances.

Additionally, as noted in the comment to point (B), all credit institutions are required to operate within the parameters set by the EU Council Decision (2008/475/EC) and Commission Regulation (219/2008) with respect to the undertaking of financial transactions with Iran or persons in Iran.

(E) Deny any requests by Iranian banks to establish a subsidiary, branch, or representative office in Malta;

The establishment of a subsidiary, branch or representative office in Malta by a foreign institution is governed by Banking Rule BR/01/2008.02 issued by the MFSA and the criteria under the Banking Act, Cap. 371. Banking Rule BR/01 establishes the criteria for licensing purposes which, inter alia, includes the & fit and proper⁸ and due diligence tests.

More specifically, clause 20 of BR/01 states that an applicant for a banking licence must satisfy the MFSA that all qualifying shareholders, controllers and all persons who will effectively direct the business of the bank are suitable, fit and proper persons. These criteria go beyond questions of the suitability of particular individuals but entail the observance by the institution as a whole of the highest professional, ethical and business standards in conducting its activities in a prudent manner. In this respect the MFSA draws the attention of an applicant for a licence to article 32 of the Banking Act. Article 32 prohibits persons who, among other things, are interdicted or incapacitated or who have been involved in money laundering or found guilty of a crime affecting public trust, theft, fraud, extortion or of knowingly receiving property obtained by theft or fraud, from holding office within a bank.

Clause 20 similarly applies to subsidiaries and branches. In considering whether to authorise the establishment of a

subsidiary or branch the MFSA will take into consideration the nationality of the applicant to determine whether it is a suitable person. In the light of the FATF statements, therefore, nationals or institutions from Iran would not be considered by the MFSA as being fit and proper persons for the purposes of the MFSA's licensing criteria. In fact the MFSA has recently discouraged a potential request for the establishment in Malta of a representative office of an Iranian credit institution.

(F) Deny requests by Iranian FIs to enter into joint ventures with or purchase a controlling stake in any local financial institution;

Further to the conditions laid down by Article 20 of BR/01/2008.02 as detailed in item E above, Article 13 of the Banking Act establishes the criteria for participation in a credit institution. The consent of the MFSA is required for a person or entity to acquire or divest of a qualifying or a significant shareholding in a credit institution. A significant shareholding is defined as a holding of at least 5% of an entity's equity while a qualifying shareholding is at least 10%. Moreover, if as a result of an acquisition of shares in a credit institution, that institution becomes a subsidiary of the person or entity acquiring the shares, and that person is a credit institution authorized in another country, the MFSA needs to consult with the relevant authorities of the country concerned. Article 13 further provides the MFSA with the authority to deny such applications. Similar provisions are found in other financial legislation governing the non-bank financial sector.

The MFSA is therefore confident that the above statutory criteria are sufficiently robust to enable it to adequately verify the risks that such potential venture/acquisition would place on the target institution itself and on the local financial system in general.

(G) Warn those commercial sectors with significant business ties with Iran that transactions with individuals or entities from Iran have a heightened risk of money laundering or terrorist financing.

As explained above, the FIAU places the FATF statements and other similar communications in this regard on its website and, in certain cases, opts to inform credit and financial institutions individually about specific documents issued in relation to this matter. Similarly, sanctions imposed by the European Union and by the United Nations Security Council are posted on the MFSA website. Furthermore the FIAU and the MFSA ensure that the matters discussed in this paper feature prominently during any seminars, conferences or other training programmes in which they participate.

End Text

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